



**U.S. Department of the Interior
Office of Inspector General**

ADVISORY LETTER

SELECTED ASPECTS OF THE OPERATION OF THE UNITED MINE WORKERS OF AMERICA COMBINED BENEFIT FUND

**REPORT NO. 01-I-188
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United States Department of the Interior

OFFICE OF INSPECTOR GENERAL
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ADVISORY LETTER

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Memorandum

To: Director, Office of Surface Mining Reclamation and Enforcement

From: Roger La Rouché *Roger LaRouche*
Assistant Inspector General for Audits

Subject: Advisory Letter on Selected Aspects of the Operation of the United Mine Workers of America Combined Benefit Fund (No. 01-I-188)

This letter addresses our analysis of selected aspects of the operation of the United Mine Workers of America Combined Benefit Fund (CBF) for fiscal years 1996 through 2000, including the annual transfer of funds from the Abandoned Mine Reclamation Fund. The review was requested by the former Director, Office of Surface Mining Reclamation and Enforcement (OSM), who asked that we (1) evaluate the overall financial condition of the CBF, (2) determine whether the fund transfer process could be accomplished more efficiently, and (3) determine whether administrative costs are an authorized charge to the transfer bill. The OSM transferred funds to the CBF to pay the health care premiums of beneficiaries whose premiums are not assigned to coal companies. The scope of our review was limited to analyzing information necessary to respond to the former Director's questions and was not sufficient to offer an opinion on the accuracy of the CBF's financial statements in accordance with generally accepted accounting principles.

We concluded that the CBF may not be able to meet its long-term financial obligations. In addition, while we determined that the amounts transferred from the Abandoned Mine Reclamation Fund to the CBF for fiscal years 1996 through 2000 were generally accurate, we believe that the preparation of the annual transfer bill needs to be simplified to make the process more efficient and less prone to error. Finally, we believe that administrative costs are an authorized charge to the transfer bill. (These three matters are discussed in detail beginning on page 3.)

BACKGROUND

The CBF is a private employee benefit trust fund that provides health care and death benefits for eligible union coal mine workers who retired on or before July 20, 1992 and their dependents. The United Mine Workers of America Health and Retirement Funds (UMWAF), with administrative offices located in Washington, D.C., manages the CBF under the direction of a seven-member board of trustees.

The CBF was created by the Coal Industry Retiree Health Benefit Act of 1992 (26 U.S.C. § 9701-9722), replacing two health benefit plans established in 1950 and 1974 that were experiencing severe financial difficulties. Commonly known as the Coal Act, this legislation holds coal operators and related companies responsible for paying monthly premiums for the costs of health benefits relating to their retired mine workers and dependents (known as "assigned" beneficiaries). In addition, if the OSM transfer explained in the paragraphs that follow is insufficient, coal operators and related companies are required to pay a monthly premium for the health care costs of retired mine workers (and dependents) who were employed by coal operators that are no longer in business, have no related successor company, or whose former employer cannot be identified (known as "unassigned" beneficiaries). Also, these companies pay a premium for the death benefits covering all beneficiaries. As of October 1999, the CBF served a total population of 65,261, consisting of 48,289 (74 percent) assigned beneficiaries and 16,972 (26 percent) unassigned beneficiaries.

Under the Coal Act, the Social Security Administration (SSA) is responsible for computing the per beneficiary health premium and for assigning the retired mine workers to their former employers or related companies. In September of each year, the SSA provides this information to the UMWAF, where the list of assigned beneficiaries is reviewed and adjusted as necessary. The UMWAF computes the premium liability for each coal operator by multiplying the per beneficiary health premium by the number of assigned beneficiaries, and the UMWAF issues the bills to the operators on a monthly basis. At the beginning of fiscal year 2000, the UMWAF prepared a total of 401 premium assessment bills for coal operators and related companies.

Although the Coal Act obligates operating coal companies to pay the health care premiums for unassigned beneficiaries, the Act provides for a Federal subsidy. Specifically, the Coal Act authorizes a transfer of up to \$70 million of the interest earned on the principal balance of the Abandoned Mine Reclamation Fund (AML Fund)¹ in a fiscal year to the CBF to pay the estimated expenditures of unassigned beneficiary premiums. If interest is not sufficient to cover the estimated expenditures, the OSM may access a reserve consisting of interest earned from October 1, 1992 through September 30, 1995. In accordance with the Coal Act, the OSM has completed the transfers to the CBF at approximately the beginning of each fiscal year since fiscal year 1996. From fiscal years 1996 through 2000, the OSM transferred \$233.8 million to the CBF. The amounts transferred are based on bills submitted by the UMWAF, which include current medical and administrative costs, as well as any adjustments to these costs for prior years.

¹The Surface Mining Control and Reclamation Act of 1977 established the Abandoned Mine Reclamation Fund (30 U.S.C. §1231) for the purpose of reclaiming and restoring land and water resources adversely affected by past coal mining. Contributions to this fund are derived from fees assessed on coal operators for each ton of coal produced. As manager of the Abandoned Mine Reclamation Fund, the OSM invests the unappropriated balance of the fund in short-term U.S. Treasury bills. The Abandoned Mine Reclamation Fund is commonly referred to as the AML Fund.

With an average beneficiary age of 78 and the CBF statutorily closed to additional retirees, the population served by the CBF gradually decreases in size upon the deaths of the beneficiaries. To illustrate, the population of about 112,000 beneficiaries at the CBF's creation in 1992 decreased to 65,261 as of October 1999, during which time the annual mortality rate of the beneficiaries rose from 5 percent to about 8 percent. An analysis prepared by the UMWAF's actuarial consultant projected that the CBF will serve a diminishing number of beneficiaries each year, estimating that the CBF will have 337 beneficiaries in 2045.

FINANCIAL CONDITION OF THE CBF

The financial condition of the CBF has deteriorated since the mid-1990s, and should this trend continue, the CBF may not be able to meet its future financial obligations. This situation developed primarily because the monthly premiums billed to the coal operators for the assigned beneficiaries are significantly less than the costs actually incurred for their health care. In contrast, the Coal Act provides for the full recovery of medical and administrative costs incurred for the unassigned beneficiaries, which is accomplished by a transfer of funds from the interest earned on the Abandoned Mine Reclamation Fund. Accordingly, the financial problems of the CBF are not attributable to the costs associated with unassigned beneficiaries or the OSM's transfer of funds.

Under the Coal Act, the SSA computes the per beneficiary premium from which the UMWAF determines the premium liability for the coal operators based on the number of beneficiaries assigned to each operator. Since fiscal year 1996, however, the per beneficiary premium for the assigned beneficiaries has been less than the health costs, and the disparity has increased in subsequent years, as shown in Table 1.

Table 1. Per Beneficiary Premium Analysis

| Description | Fiscal Year | | | | |
|-----------------------------------|--------------|--------------|--------------|------------------------|------------------------|
| | 1996 | 1997 | 1998 | 1999 | 2000 |
| Actual cost per beneficiary | \$2,219 | \$2,497 | \$2,919 | \$3,316 (Estimated) | \$3,562 (Estimated) |
| Premium set by SSA | <u>2,200</u> | <u>2,280</u> | <u>2,343</u> | <u>2,420</u> | <u>2,503</u> |
| Difference (unrecovered costs) | \$19 | \$217 | \$576 | \$896 | \$1,059 |

We believe the two principal reasons accounted for the variance between the actual costs per beneficiary and the premiums set by SSA. First, as prescribed by the Coal Act, the SSA computes the premium on the basis of the actual payments provided to beneficiaries under the

1950 and 1974 health benefit plans for the year beginning July 1, 1991, with annual adjustments for inflation based on the Consumer Price Index. This inflation factor represents the cost increases associated with the health care of the general public and does not accurately adjust for the additional costs incurred for the CBF population, which is much older than the general population and requires greater levels of medical care. For example, the elderly generally have a greater need for prescription drugs, and the costs of prescription drugs have significantly exceeded the costs of other medical services provided in recent years. Therefore, the premium does not take into account these increased costs for the CBF.

Second, a lawsuit brought by an association of coal industry employers and several assigned operators challenged the methodology on which the SSA had based its premium computations since 1993. The principal change was to adjust the amount actually received by the UMWAF for Medicare reimbursements. The resulting court decision² in July 1995 reduced the premiums charged the coal operators by about 10 percent. In addition, subsequent legal actions on this matter resulted in the UMWAF's establishing a reserve to refund about \$37 million to the coal operators for the differential amounts between the premiums actually collected and the premiums recalculated in accordance with the court order. Consequently, these legal actions have further reduced the revenues available for the CBF.

The effect that the shortfall in the premium assessment for assigned beneficiaries has on the CBF is illustrated in Table 2.

Table 2. Unrecovered Health Costs

| <u>Description</u> | <u>Fiscal Year</u> | | | |
|---|--------------------|-------------|-------------|----------------------|
| | <u>1996</u> | <u>1997</u> | <u>1998</u> | <u>1999</u> |
| Assigned beneficiaries | 70,307 | 63,414 | 58,556 | 52,324 |
| Multiplied by the difference in per beneficiary premium (see Table 1) | \$19 | \$217 | \$576 | \$896 (Estimated) |
| Unrecovered costs (in millions) | \$1.3 | \$13.8 | \$33.7 | \$46.9 |

As shown in Table 2, the costs of providing health care for the assigned beneficiaries have exceeded the revenues generated at an increasing rate. As a result, the CBF's available financial resources to compensate for the shortfall have gradually declined, as shown in Table 3.

²National Coal Association v. Chater, Northern District of Alabama, July 1995. Upheld by the Eleventh Circuit Court of Appeals (81 F.3d 1077) in 1996.

Table 3. CBF Net Asset Balance

| | Fiscal Year | | | |
|------------------------------------|-------------|-------------|-------------|-------------|
| | <u>1996</u> | <u>1997</u> | <u>1998</u> | <u>1999</u> |
| Net asset balance (in millions) | \$111.1 | \$95.5 | \$24.7 | (\$12.2) |

In fiscal year 1999, the financial statements for the CBF showed a deficit asset balance for the first time. In addition, the actuarial consultant for the UMWAF reported in April 2000 that the deficit will grow in future years, estimating the deficit to be \$611.5 million at the end of fiscal year 2009.

In an effort to maintain the solvency of the CBF, the President and the Congress have taken actions in recent years to provide special appropriations for the fund. Specifically, \$68 million was appropriated in fiscal year 2000 from the AML Fund interest reserve,³ and the President's proposed budget for fiscal year 2001 contained a \$49 million appropriation from the general fund in addition to the regular OSM transfer, with a total of \$346 million to be provided over the next 10 years. The proposed budget would also reverse the reduction in the premium that was caused by the court decision in National Coal Association v. Chater. Further, a bill was introduced in March 2000 in the U.S. House of Representatives (H.R. 4144) and approved by the House Resources Committee in July 2000 that would appropriate an additional \$96.8 million from interest accumulated on the AML Fund.

We examined the potential effect of the special appropriations on the long-term solvency of the CBF. Our analysis was based on the actuarial projections of the UMWAF's consultant for the CBF, and we assumed that the level of medical benefit coverage provided to beneficiaries would not change and that no additional funding assistance would be provided. Our analysis disclosed that the financial support provided by these special appropriations may not be sufficient to ensure the long-term solvency of the CBF. More specifically, we concluded that if both of the special appropriations are enacted, the CBF should maintain a positive asset balance through about fiscal year 2005.

We believe that CBF trustees, coal operators, the UMWAF, and cognizant Federal agencies should work together to address the issue concerning the long-term solvency of the CBF. For example, a committee similar to the Coal Commission⁴ in 1990 could be convened to monitor and recommend solutions for the beneficiaries' health care. Two solutions that should be considered are (1) amending the Coal Act to require that the per beneficiary premium charged

³The reserve of the AML Fund had accumulated \$132.5 million in interest as of September 30, 1995. In December 1999, the OSM, at the direction of the Department of the Interior and Related Agencies Appropriations Act of 2000, transferred \$68 million from the reserve to cover a shortfall in CBF premium accounts. As a result of the transfer, the reserve had a balance of \$64.5 million as of June 1, 2000.

⁴The Coal Commission included representatives of the coal industry, coal employees, the health insurance industry, the medical profession, academia, and the government.

for the assigned beneficiaries equals the costs actually incurred for the beneficiaries' health care and (2) increasing the level of financial support from Federal sources. If the financial condition of the CBF does not improve, it may become necessary to reduce the amount of health care benefits provided to the beneficiaries to a level commensurate with premiums collected.

IMPROVEMENTS FOR THE TRANSFER PROCESS

The process of computing the annual transfer bill was very complex, and as a result, the transfer bills were vulnerable to error and delay as follows:

- The transfer bills for fiscal years 1999 and 2000 had several computational errors that resulted in net understated transfers of \$885,000 and \$427,000, respectively, or about 1 percent of the transfer bills. Although these amounts did not represent a material misstatement of the bills, the potential exists for errors to occur that are more significant in amount. Moreover, the potential for errors increases each year because the bill, which may contain adjusted data⁵ for transfers made in prior years, continuously grows in detail and complexity. During our discussions in March 2000, UMWAF officials agreed to conduct an independent verification of the transfer bill and supporting computational worksheets before submitting the bill to the OSM. Although this quality control review should improve the accuracy of the bill, the complexity of the bill will continue to grow indefinitely because prior year transfers remain subject to future adjustment. For example, the bill for fiscal year 2000 included adjustment computations for the amounts transferred in each of the previous 4 years. In turn, the bill for fiscal year 2001 may include adjustments for the previous 5 years.

- Because the SSA was approximately 1 month late in submitting the list of unassigned beneficiaries for the fiscal year 2000 transfer, the UMWAF was unable to prepare the transfer bill in a timely manner. Consequently, the OSM was more than 1 month late in executing its transfer. We attributed the delay to the assignment provisions of the Coal Act, which require the SSA to assign each retired coal worker to the coal operator or related company that employed the worker. This is a complicated and time-consuming process, since each of the approximately 65,000 beneficiaries (coal workers and their dependents) that make up the CBF population are subject to reclassification because of appeals and litigation from the coal operators. Additionally, if a worker or a dependent is reclassified in one year, all other years are also subject to adjustment.

We believe that an alternative approach for determining the transfer amount should be considered and that the principal parties involved in the transfer (UMWAF, OSM, and SSA) should work together to identify a more efficient process. We also believe that the UMWAF, as the union which represents the retired mine workers, and the coal operators, as the original funding source for the health care of all CBF beneficiaries, should participate in this endeavor.

⁵Adjustments are necessary, for example, to revise the number of unassigned beneficiaries, to update health care cost data, or to correct computational errors made in prior transfer bills.

The coal operators pay the health care costs in two ways. First, the costs related to assigned beneficiaries are billed to the operators through direct premium assessments. Second, although the OSM makes the interest transfer to pay the costs related to unassigned beneficiaries, the AML Fund from which the interest is earned is derived from the coal industry through tonnage assessments on the coal produced.

One suggestion to simplify and expedite the fund transfer would involve eliminating the detailed computations associated with the preparation of the transfer bill. That is, assuming that the transfer bill stabilizes in amount, future bills could be based on an average amount or an extrapolation of prior year transfers. An adjustment to the transfer bill would be necessary only to reflect the declining population of the unassigned beneficiaries.

ADMINISTRATIVE COSTS

The OSM has paid the full amount of administrative costs contained in each transfer bill since fiscal year 1996 in accordance with a memorandum of understanding with the UMWAF. However, OSM officials recently questioned this practice based on (1) the "Congressional Record" (138 Cong. Rec. §17578 and 17604) for the Coal Act, which states that "only assigned operators are responsible for paying the Combined Fund's cost of providing benefits" and (2) a December 29, 1999 letter from the Office of the Solicitor to the Director of Budget, Department of the Interior, which stated, "We could support the position that the costs of providing benefits under the CBF should be borne by the assigned operators." The OSM also asked that we examine this issue.

Based on our review, we concluded that the transfer bill should include administrative costs. The Coal Act, which amended the Surface Mining Control and Reclamation Act (30 U.S.C. § 1232(h)) to provide for the transfer from the Abandoned Mine Reclamation Fund, stipulates that the transfer not exceed the amount of the expenditures recorded for the CBF's unassigned beneficiaries premium account. This account, established under the Coal Act (26 U.S.C. § 9704(e)), consists of the unassigned beneficiaries premiums and an allocation of administrative costs. Therefore, notwithstanding the legislative history contained in the "Congressional Record," the actual language of the applicable laws requires the transfer to include administrative costs.

Further, when considered in its full context, we believe that the "Congressional Record" statement does not preclude administrative costs from being paid. The statement that the assigned operators are responsible for paying the costs of providing benefits merely recognizes that the Congress intended the assigned coal operators and the related companies to assume primary financial responsibility for the CBF. The Congress did not want the OSM to assume any role in the transfer process other than as a funding source to subsidize the health premium costs relating to unassigned beneficiaries.

To illustrate, the "Congressional Record" (138 Cong. Rec. § 17578 and 17603) states, "The essence of the Conference Agreement is that those companies which employed the retirees in question, and thereby benefitted from their services, will be assigned responsibility for providing the health care benefits promised in their various collective bargaining agreements." In reference to the annual transfer made by the OSM, the "Congressional Record" (§ 17578 and 17605) further states, "This money may be used solely for the purpose of subsidizing the cost of providing health care to unassigned beneficiaries." In summary, consistent with this legislative history and as required by the Coal Act, we believe that the OSM is obligated to include administrative costs in the transfer.

Since this letter does not contain any recommendations, a response is not required.

This advisory letter will be listed in our semiannual report to the Congress, as required by Section 5(a) of the Inspector General Act (5 U.S.C. app. 3).

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